

BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 2021-153-S- ORDER NO. 2021__

DECEMBER ____, 2021

IN RE: Application of Palmetto Wastewater)
 Reclamation, Incorporated for an)
 Adjustment of Rates and Charges) **PROPOSED ORDER**

I. INTRODUCTION AND PROCEDURAL HISTORY

This matter comes before the Public Service Commission of South Carolina (“Commission”) pursuant to S.C. Code Ann. §§ 58-5-10(4), 58-5-210, 58-5-240, and S.C. Code Ann. Regs. 103-512.4.A and 103-503 for approval of the monthly sewer service charges and rate schedule language changes set forth in the application (“Application”) and rate schedules filed by Palmetto Wastewater Reclamation, Inc. (“PWR,” “Palmetto,” or the “Company”).

Consistent with S.C. Code Ann. § 58-5-240(A), PWR filed a letter with the Commission on May 3, 2021, regarding its intent to file the Application and proposed rate schedule seeking an adjustment in the Company’s rates and charges, as well as the terms and conditions of sewer service. The South Carolina Office of Regulatory Staff (“ORS”) filed a Notice of Appearance for Christopher M. Huber and Jenny R. Pittman on May 18, 2021.¹ The Commission Clerk’s Office filed a Proposed Customer Bill Insert Timeline (“Timeline”) on June 1, 2021, which identified the proposed dates for newspaper publication and procedural dates assuming the Application was filed on June 3, 2021. During email correspondence that took place that same day, the Company notified the Commission that the Application would be filed no later than June 16, 2021, and PWR would

¹ ORS, by statute, is automatically a party to the proceeding. S.C. Code Ann. § 58-4-10(B).

propose a revised schedule. ORS and the South Carolina Department of Consumer Affairs (“DCA”) filed comment letters in response to the Timeline on June 3, 2021. The Timeline came before the Commission at the June 9, 2021, business meeting; the matter was carried over and no vote was taken.

The DCA filed a Notice of Appearance for Carrie Grube Lybarker, Roger P. Hall, and Connor J. Parker on June 11, 2021.

The Company, ORS, and the DCA (“the Parties”) collaboratively proposed a schedule (“Joint Schedule”) to the Commission identifying dates for notice and pre-filed testimony on June 11, 2021.

PWR filed its Application for an adjustment of its rates and charges on June 16, 2021. The Application was filed pursuant to S.C. Code Ann. § 58-5-240 and S.C. Code Ann. Regs. 103-512.4.A. In its Application, PWR sought approval of an increase in the monthly sewer service charge to \$43.12 for residential customers and single family equivalents (“SFE”) for commercial customers, an increase to \$32.18 for mobile home customers; rate base treatment; an increase to the tampering charge to an amount not to exceed \$500 for a customer who damages or tampers with utility property; and a proposed a test year beginning January 1, 2020 and ending December 31, 2020.

The Commission issued Directive Order No. 2021-434 dated June 17, 2021, approving a bill insert timeline.

The DCA filed a Petition to Intervene on June 18, 2021, pursuant to its authority under S.C. Code Ann. § 37-6-604 to provide representation of the consumer interest before state and federal regulatory agencies when such agencies undertake to fix rates or prices for consumer

products or service and may intervene as a party to advocate for the interests of consumers before the Commission.²

On June 30, 2021, the Commission issued a Notice of Filing and Public Hearings (“Notice”) which outlined the proposed changes in rates and charges for each customer class, gave notice to customers about the public hearings for customers to provide testimony on the Company’s Application, and informed the public as to the date for the merits hearing in this docket. By letter dated that same day, the Clerk’s Office instructed the Company to (i) publish the Notice in newspapers of general circulation by July 16, 2021, and (ii) provide Proof of Publication by September 6, 2021. The Clerk’s Office further instructed PWR to provide the Notice to each affected customer via bill inserts or by electronic mail to those customers who have agreed to receive notices by electronic mail on or before August 16, 2021, and to provide certification of such on or before September 6, 2021. Finally, the Clerk’s Office instructed the Company to provide the Notice to the County Administrator in any county that PWR provides services as well as the City Administrator in any city where the Company provides services, and to provide certification of such on or before September 6, 2021. The Clerk’s Office also issued a letter dated June 30, 2021, with deadlines for pre-filed testimony, as well as the date for notifying the Commission regarding the order of each party’s witnesses to be presented during the hearing, any objections to taking direct and rebuttal or surrebuttal testimony together during the hearing, and if any party to the proceeding wants to use panels of witnesses.

On July 13, 2021, the Company filed with the Clerk’s Office an Affidavit and tear sheet reflecting publication of the Notice in a general circulated newspaper. Two days later, on July 15,

² The Commission granted the DCA’s Petition to Intervene on August 31, 2021; *See* Order No. 2021-113-H.

2021, the Company filed with the Clerk's Office the letters containing the Notice sent to the Lexington County Administrator, Richland County Administrator, Irmo City Administrator, and the Columbia City Manager. By letter dated July 22, 2021, the Company notified the Commission that practical considerations would prohibit the Company from furnishing its affected customers with a copy of the Notice of Filing via bill inserts by the date set by the Commission. The Company, to comply with the Commission's instructions, would provide each affected customer with a copy of the Notice via U.S. Mail by August 16, 2021. PWR provided the affidavit of April Braswell, the billing manager for the Company who attested that each affected customer was sent the Notice on July 21, 2021, via U.S. Postal Service First Class Mail.

ORS filed a Revised Notice of Appearance of Counsel for Christopher M. Huber and Nicole M. Hair on July 29, 2021.

On September 2, 2021, PWR filed the prefiled direct testimony of Witnesses Craig Sorensen, Donald H. Burkett, and Mujeeb Hafeez and the prefiled direct testimony, appendix, and exhibit of Witness Paul R. Moul.³ The Company moved for protective treatment regarding certain confidential information contained within Mr. Hafeez's testimony,⁴ and filed a redacted version of his testimony with the Commission.

On September 7, 2021, ORS filed a Motion to Compel Production of Documents and Things ("Motion"). Specifically, ORS requested the Commission compel production of copies of the minutes of SouthWest Water Company's ("SWWC") Board of Directors meetings that occurred during calendar year 2019 and all presentations made to SWWC's Board during calendar year 2019. PWR is a subsidiary of SWWC, which allocates costs for shared products and services

³ Mr. Hafeez's prefiled direct testimony included four attachments.

⁴ The Commission granted the Company's request on September 15, 2021. *See* Order No. 2021-626.

provided by SWWC to its affiliates such as PWR. Among the costs allocated are ones associated with SWWC's Board. The Company filed a Return to ORS's Motion on September 17, 2021. ORS filed a Reply in Support of its Motion on September 21, 2021. In Directive Order No. 2021-640, the Commission granted ORS's Motion and ordered the Company to provide ORS with the materials requested within ten (10) days of receipt of the Order. PWR complied with Order No. 2021-460.

The DCA filed the prefiled direct testimony and exhibits of Witnesses Aaron Rothschild and Lafayette Morgan, Jr., on September 30, 2021. ORS filed the prefiled direct testimony and exhibits of David J. Garrett, Daniel P. Hunnell, and Christina L. Seale that same day.⁵

On October 14, 2021, the Company filed the prefiled rebuttal testimony of Witnesses Paul R. Moul, Mujeeb Hafeez, Craig Sorensen, and Donald H. Burkett. The Company filed corrected rebuttal testimony of Witness Craig Sorensen on November 9, 2021.

On October 28, 2021, ORS filed the prefiled surrebuttal testimony and exhibits of Witnesses Christina L. Seale and Daniel P. Hunnell, and the surrebuttal testimony of David P. Garrett. The DCA filed the prefiled surrebuttal testimony of Aaron Rothschild and Lafayette Morgan Jr. Witness Morgan's surrebuttal testimony was accompanied by thirteen (13) schedules. The DCA filed corrected surrebuttal testimony for Witness Rothschild on November 10, 2021.

The Commission conducted a public hearing in this matter on Monday, November 8, 2021, beginning at 9:00 a.m., with the Honorable Justin T. Williams presiding. One PWR customer came forward to provide comments on the Application. With no additional witnesses having registered

⁵ ORS filed a redacted, public version of Witness Garrett's direct testimony and exhibits and a confidential, unredacted version because the testimony contained information PWR had designated confidential.

to speak, the Commission suspended the hearing and cancelled the remaining hearings originally scheduled in this docket.

On November 10, 2021, ORS filed a Partial Stipulation (“Stipulation”) signed by the Parties. The Stipulation is attached hereto as Exhibit 1.⁶ The Stipulation constituted an agreed compromise of all positions advanced by the Parties with the exception of the authorized return on equity (“ROE”). The Stipulation provided that the Parties agreed to stipulate into the record the pre-filed testimony and exhibits of certain witnesses without objection, change, amendment, or cross-examination.⁷ The other terms of the Stipulation are described in further detail below.

The merits hearing began on November 10, 2021, beginning at 10:00 a.m., with the Honorable Justin T. Williams presiding. Due to the ongoing COVID-19 pandemic, certain parties and witnesses appeared remotely.⁸ Charles L.A. Terreni, Esquire, and Scott Elliott, Esquire represented the Company. Nicole M. Hair, Esquire and Christopher M. Huber, Esquire represented ORS. Roger P. Hall, Esquire and Connor J. Parker, Esquire represented the DCA.

At the start of the hearing, the Stipulation was accepted into the record as Hearing Exhibit 1. Those witnesses who were not otherwise excused from appearing at the merits hearing were sworn in and their prefiled testimonies were accepted into the record, including any corrections, accompanying exhibits and appendices, and confidential versions filed under seal.⁹ ORS Witness

⁶ Tr. p. 48, Hearing Ex.2 (“Stipulation”)

⁷ The Parties agreed to stipulate into the record the testimony and exhibits of PWR Witnesses Donald H. Burkett and Mujeeb Hafeez, DCA Witness Lafayette Morgan, Jr., and ORS Witnesses Christina L. Seale. Witnesses Burkett, Hafeez, Morgan, and Seale were excused from presenting their testimony in-person. Verifications were provided by the respective Parties for these witnesses.

⁸ Company Witness Moul testified virtually. DCA Attorneys Roger P. Hall and Connor J. Parker appeared virtually, as did DCA Witness Rothschild. For ORS, Witness Garrett testified virtually. *See* Order No. 2021140-H.

⁹ The Parties stipulated to, and the Commission accepted Witnesses Moul, Garrett, and Rothschild as experts on the fair rate of return for a regulated utility, including its cost of debt, return on equity, and capital structure. The Parties also stipulated to, and the Commission accepted Witness Garrett as an expert on customer financial protections known as ring fencing. In addition, the Parties stipulated to, and the Commission accepted Witness Hunnell as an expert in utility ratemaking and regulatory analysis.

Hunnell was presented for questions from the Commission but was not cross-examined by counsel for the Company or the DCA as agreed to pursuant to the Stipulation. Company Witnesses Sorensen and Moul, DCA Witness Rothschild, and ORS Witness Garrett were presented for cross-examination from the other parties and questioning from the Commission.

II. STATUTORY STANDARDS AND REQUIRED FINDINGS

The Company's current rates now in effect were approved in Commission Order No. 2019-314 issued on May 14, 2019, in Docket No. 2018-82-S. The Company is a public utility, as defined by S.C. Code Ann. § 58-5-10(4), providing sewer service to the public for compensation in certain areas of Richland and Lexington Counties. Application ¶ 2. The Company proposes a test year of January 1, 2020, to December 31, 2020. Application ¶ 5.

The Application, testimony, exhibits, affidavits of publication, and public notices submitted by the Company comply with the procedural requirements of the South Carolina Code of Laws and the Regulations promulgated by this Commission.

South Carolina Code Ann. § 58-5-210 provides, “[t]he Public Service Commission is hereby...vested with power and jurisdiction to supervise and regulate the rates and service of every public utility in this State, together with the power, after hearing, to ascertain and fix such just and reasonable standards, classifications, regulations, practices and measurements of service to be furnished, imposed, observed and followed by every public utility in this State and the State hereby asserts its rights to regulate the rates and services of every ‘public utility’ as herein defined.” “[R]ate-making is not an exact science, but a legislative function involving many questions of judgment and discretion.” *Parker v. S.C. Pub. Serv. Comm'n*, 280 S.C. 310, 312, 313 S.E.2d 290, 291 (1984).

The object of using test year figures is to reflect typical conditions. The Company has the benefit of choosing its test year. Where an unusual situation indicates that the test year figures are atypical, the Commission should adjust the test year data. *Parker v. S.C. Pub. Serv. Comm'n*, 280 S.C. 310, 312, 313 S.E.2d 290, 292 (1984). “[A]djustments for known and measurable changes in expenses may be necessary in order that the resulting rates reflect the actual rate base, net operating income, and cost of capital. The adjustments are within the discretion of the Commission and must be known and measurable within a degree of reasonable certainty. Absolute precision, however, is not required.” *Hamm v. S.C. Pub. Serv. Comm'n*, 309 S.C. 282, 291, 422 S.E.2d 110, 115 (1992) (citing *Michaelson v. New England Tel. & Tel. Co.*, 404 A.2d 799 (R.I. 1979)).

“Although the burden of proof of the reasonableness of all costs incurred which enter into a rate increase request rests with the utility, the utility’s expenses are presumed to be reasonable and incurred in good faith. This presumption does not shift the burden of persuasion but shifts the burden of production on to the . . . contesting party to demonstrate a tenable basis for raising the specter of imprudence. . . . The ultimate burden of showing every reasonable effort to minimize . . . costs remains on the utility.” *Utils. Servs. of S.C., Inc. v. S.C. Pub. Serv. Comm'n*, 392 S.C. 96, 109–10, 708 S.E.2d 755, 762–63 (2011) (quoting *Hamm v. S.C. Pub. Serv. Comm'n*, 309 S.C. 282, 286, 422 S.E.2d 110, 112 (1992)). The Commission has the “powers to ‘to supervise and regulate’ rates and service and ‘to fix just and reasonable standards, classifications, regulations, practices, and measurements of service.’” *Id.* at 105, 708 S.E.2d at 760 (quoting S.C. Code Ann. § 58-3-140(A)). “Pursuant to these powers, the PSC is entitled to create incentives for utilities to improve their business practices.” *Id.* “Accordingly, the PSC may determine that some portion of an expense actually incurred by a utility should not be passed on to consumers.” *Id.*

The Commission, as an administrative agency, “is generally not bound by the principle of stare decisis but it cannot act arbitrarily in failing to follow established precedent.” *See* 330 *Concord St. Neighborhood Ass’n v. Campsen*, 309 S.C. 514, 517–18, 424 S.E.2d 538, 539–40 (Ct. App. 1992).

Pursuant to S.C. Code Ann. § 58-3-60, “[t]he commission shall not inspect, audit, or examine public utilities. The inspection, auditing, and examination of public utilities is solely the responsibility of the Office of Regulatory Staff.”

The Commission must consider the evidence presented to it on the formal record. “Because the PSC is both entitled and required to consider the evidence presented to it on the formal record, the PSC is entitled to rely on sworn testimony presented by non-party protestants to overcome the presumption of reasonableness.” *Utils. Servs.*, 392 S.C. at 111, 708 S.E.2d at 763.

The Commission must determine a fair rate of return that the utility should be allowed the opportunity to earn after recovery of the expenses of utility operations. The legal standards for this determination are set forth in *Federal Power Comm’n v. Hope Natural Gas Co.*, 320 U.S. 591, 602-03(1944) (“*Hope*”) and *Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679, 692-93 (1923) (“*Bluefield*”).

In *Bluefield*, the United States Supreme Court held that:

What annual rate will constitute just compensation depends upon many circumstances, and must be determined by the exercise of a fair and enlightened judgment, having regard to all relevant facts. A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support

its credit and enable it to raise the money necessary for the proper discharge of its public duties. A rate of return may be reasonable at one time and become too high or too low by changes affecting the opportunities for investment, the money market and business conditions generally.

Bluefield, 262 U.S. at 692-93.

The Commission and South Carolina appellate courts have consistently applied the principles set forth in *Bluefield* and *Hope*. See *Southern Bell Tel. & Tel. Co. v. Pub. Serv. Comm'n of S.C.*, 270 S.C. 590, 244 S.E. 2d 278 (1978). Quoting *Hope*, the South Carolina Supreme Court has stated: “‘under the statutory standard of ‘just and reasonable’ it is the result reached not the method employed which is controlling.... The ratemaking process under the Act, i.e., the fixing of ‘just and reasonable’ rates, involves the balancing of investor and the consumer interests.’” *So. Bell*, 270 S.C. at 596, 244 S.E.2d at 281 (quoting *Hope*, 320 U.S. at 602-03).

This Commission must exercise its dual responsibility of permitting utilities an opportunity to earn a reasonable return on the property it has devoted to serving the public, on the one hand, and protecting customers from rates that are so excessive as to be unjust or unreasonable, on the other, by “(a) Not depriving investors of the opportunity to earn reasonable returns on the funds devoted to such use as that would constitute a taking of private property without just compensation[, and] (b) Not permitting rates which are excessive.” *So. Bell*, 270 S.C. at 605, 244 S.E. 2d at 286 (Ness, J., concurring and dissenting).

Additionally, the Commission’s determination of a fair rate of return must be documented fully in its findings of fact and based exclusively on reliable, probative, and substantial evidence on the whole record. *Porter v. S.C. Pub. Serv. Comm’n*, 332 S.C. 93, 98, 504 S.E.2d 320, 323 (1998). In making its decision, the Commission cannot make a determination based upon surmise,

conjecture or speculation. *See Herndon v. Morgan Mills, Inc.*, 246 S.C. 201, 209, 143 S.E.2d 376, 380 (1965).

The findings of facts and conclusions of the Commission herein reflect these standards and the Commission employed the same upon review of the evidence in the record.

III. REVIEW OF THE EVIDENCE AND EVIDENTIARY CONCLUSIONS

A. Issues Addressed under Stipulation

Issues Addressed

The Partial Stipulation executed by the ORS, the Company, and the DCA constituted a compromise resolution of all issues except for authorized ROE. Stipulation ¶ 3, . Pursuant to the Stipulation, the Parties agreed to accept and adopt all recommendations, adjustments, and customer protections in the testimony and exhibits of ORS witnesses unless specifically modified by the Stipulation. Stipulation ¶ 4; *see also* Tr. pp. 34-35. The recommendations, adjustments, and customer protections in the testimony and exhibits of ORS witnesses accepted and adopted by the Parties include ORS's recommended adjustment related to the Company's allocation of corporate overhead and shared costs to PWR discussed in ORS Witness Seale's Direct Testimony. *Id.* The Parties agreed to the correction in ORS Adjustment 3 regarding depreciation expenses described in ORS Witness Seale's Surrebuttal Testimony and revenue adjustments proposed by ORS based on the actual number of customers and equivalent residential customers by class as of the end of August 2021. *Stipulation*, ¶ 4. The Company did not offer specific rebuttal testimony in opposition to these adjustments.

The Parties also agreed to the recommendation of ORS and the DCA to amortize rate case expenses over three years. Stipulation, ¶ 5. The Company had requested two years. The Parties

further agreed the amount of rate case expenses to be amortized over three years is \$160,000.¹⁰

Stipulation ¶ 5

In addition, the Parties agreed to amend Adjustment 2L to allow PWR recovery of the additional \$14,336 in chemicals expense requested in PWR Witness Burkett's Rebuttal Testimony. Stipulation ¶ 6; . ORS had opposed the requested additional chemical expense in Witness Seale's Surrebuttal Testimony.

Customer protections the Parties accepted under the Stipulation include those proposed by ORS Witness Garrett in his Direct Testimony related to the acquisition of Ni South Carolina, LLC (now Ni South Carolina, Inc.), the parent company of PWR, from Ni Pacolet Milliken Utilities, LLC by South Carolina Utility Systems, Inc. ("the Acquisition"). *Id.* These customer protections discussed in Witness Garrett's Testimony, also referred to as ring-fencing provisions, include PWR not seeking recovery of any goodwill associated with the Acquisition in future rate proceedings, PWR not seeking recovery of any acquisition or transaction costs associated with the Acquisition in future rate proceedings, PWR not assuming the role of guarantor for any debt of SWWC or its affiliates or subsidiary entities unless that debt is incurred for purposes specific to the PWR system and operations, that any debt incurred by PWR is and will only be used for purposes specific to the PWR system, and that PWR will not lend cash or other capital directly to SWWC or any SWWC affiliate or subsidiary entities except for routine and prudent cash management practices. *Id.* The Company did not offer specific rebuttal testimony in opposition to these recommended customer protections.

¹⁰ The Company provided documentation to ORS demonstrating \$160,000 of rate case expenses had been incurred.

The Stipulation addressed two of the three components of PWR's cost of capital: capital structure and cost of debt. The Parties did not agree to an authorized ROE in the Stipulation. Under the Stipulation, the Parties agreed to capital structure for PWR that includes 45% debt and 55% equity. Stipulation ¶ 7. In its testimony, the Company recommended adopting its test period capital structure ratio of 40.08% debt and 59.92% equity. Moul Direct p. 13; Tr. p. 139.13, ll. 3-10. ORS Witness Garrett asserted the Company's proposed capital structure was too equity-rich and increased capital costs above a reasonable level. Garrett Direct Tr. p.7, l. 17-26. ORS recommended an imputed capital structure consisting of 50% debt and 50% equity, which was equal to the proxy group in this case. *Id.* . DCA Witness Rothschild recommended a capital structure of 49.26% equity and 50.74% debt based on the average common equity ratios of the companies in his proxy group. Rothschild Direct Tr. p. 194.34, ll. 19-17.

Regarding cost of debt, the Parties agreed to a rate of 3.79% under the Stipulation. Stipulation ¶ 8. Company Witness Moul proposed a 3.79% based on the Mergent Bond Record for Baa-rated public utility bonds. Moul Direct Tr. P. 139.14, LL. 1-3. ORS did not recommend a different cost of debt. Garrett Direct p. 76; Tr. p. DCA Witness Rothschild recommended 3.20% in his Direct Testimony. Rothschild Direct, Tr. pp. 194.34-35. He updated his recommendation to 3.67% in his Surrebuttal Testimony to reflect the market yield of Baa rated corporate bonds between January 2021 and August 2021. Rothschild Surrebuttal, Tr. p. 196.15.

Regarding tariff language changes, the Company agreed to amend its Rate Schedule to remove Section 13 – Limitation of Liability and to amend the last paragraph of Section 1 – Monthly Charge to remove certain language as set forth in the Stipulation. Stipulation ¶¶ 10, 11. Additionally, the Parties agreed to PWR's request to amend Section 12 of its Rate Schedule to increase the maximum amount of its tampering charge to \$500. Stipulation ¶ 12. The DCA,

through Witness Morgan's testimony, had opposed the increase in the maximum amount of the tampering charge. Morgan Direct. p. 13-14; Transcript p. 233.ll 13-14.

The Parties agreed to various fallout adjustments to reflect the terms of the Stipulation and the ROE granted by the Commission.

Finally, PWR agreed in the Stipulation that it would not file another a general rate case before eighteen (18) months from the date the final order is issued in this proceeding, such that new rates would not be effective prior to twenty-four (24) months from the date the final order is issued. Stipulation ¶ 15.

ORS introduced into the record at the hearing an exhibit with Attachments B, C, and D showing the Operating Experience, Rate Base, and Rate of Return utilizing the terms of the Stipulation and each of the three different ROEs recommended by Witnesses Moul, Garrett, and Rothschild in this proceeding. Tr. p. 208, Hearing Ex. 8. Attachment A to this exhibit provided a summary of the revenue requirement and rates under the three different ROE's and the terms of the Stipulation. Id.

Commission Finding

The Commission as the finder of fact has carefully evaluated the evidence submitted in this case related to the issues resolved by the Stipulation. The Commission concludes that it is just and reasonable and a fair balancing of the interests of the Company and its customers to approve the Stipulation. No party opposes the Stipulation, and all Parties to this proceeding support it as a just and reasonable resolution of all issues within this proceeding except for authorized ROE.

B. Return on Equity

In its Application and testimony, Palmetto requests that the Commission determine the just and reasonableness of its proposed rates in accordance with the rate base methodology, *i.e.*, the

rate base and rate of return treatment. Palmetto's President, Craig Sorensen, and its expert witness, Paul Moul, testified in support of the Company's requested ROE. Mr. Sorensen testified that all of Palmetto's affiliates with specific ROEs approved by regulatory commissions since at least 2018 have been awarded ROEs over 9.00%. Tr. pp. 69, l. 2-70, l.3; 75.4, l. 3-7. Mr. Sorensen explained that Palmetto's efforts to attract investment capital would be disadvantaged if the Commission awarded the ROEs recommended by the ORS and DCA expert witnesses. *Id.* Sorensen also said that Palmetto's excellent record of customer service and environmental compliance justify a higher ROE. *Id.* Palmetto only had two customer complaints in the past year, both of which were quickly resolved. Tr. p. 72, l. 1-11. Only one of Palmetto's customers testified at the public hearing in this case, and she had no complaint about the company's service. *Id.*

Palmetto also presented Direct and Rebuttal Testimony of its expert witness Paul Moul, who recommended an overall rate of return for the Company, including a specific ROE.¹¹ Mr. Moul recommended an ROE of 10.95. Tr. pp. 134, l. 18-135, l. 6. Mr. Moul arrived at his recommendation using data from a proxy group of eight publicly traded water companies. Mr. Moul used water companies as proxies because there is insufficient data on wastewater utilities. Tr. pp. 139, l.1-140, l. 5. He relied on four recognized measures of the cost of equity: the Discounted Cash Flow ("DCF"), Risk Premium ("RP"), Capital Asset Pricing Model ("CAPM") and the Comparable Earnings ("CE") approach. *Id.*

Model	Cost of Equity
DCF	10.41
RP	10.50
CAPM	12.05
Comparable	12.80

¹¹ Mr. Moul was qualified as an expert on the fair rate or return for a regulated utility, including its cost of debt, return on equity and capital structure, as were Aaron Rothschild, who testified for the DCA, and David Garrett, who was called by ORS.

Earnings	
Average	11.44
Median	11.28
Mid-point	11.61

Moul averaged the market return models, DCF, RP, and CAPM to arrive at his recommendation of 10.95%. Mr. Moul also conducted a fundamental risk analysis to determine Palmetto's relative risk position in the market. Tr. p. 139.6, l. 7-16. He evaluated qualitative and quantitative factors affecting Palmetto's cost of equity. *Id.* Among the qualitative factors considered were the impact of the coronavirus pandemic, which unsettled the stock and bond markets in the spring of 2020. Tr. p. 139.2, l. 3-21. Quantitative factors considered included Palmetto's small size, .02% of the average size of a company in his proxy group. Tr. pp. 139.7, l. 21-140, l. 2. Moul also testified that Palmetto and its proxies had more leverage than the market as a whole and a greater variability in their return on equity. Tr. pp. 139.7-139-11. Palmetto itself is riskier than the proxy group. Tr. 139.11, l. 10-14. Therefore, the proxy group provides a very conservative basis for measuring Palmetto's cost of equity. *Id.*

The DCA's expert witness, Aaron Rothschild, recommended an ROE of 7.31% for Palmetto, derived from a range of 6.13% to 7.7%. Tr. p. 181, ll. 1-7. Mr. Rothschild uses current market prices to measure investor's expectations directly. Tr. p. 194.36, l. 10-12. To arrive at his recommendation, Mr. Rothschild used a Constant Growth and Non-Constant Growth DCF and a CAPM analysis. Tr. p. 194.37, ll. 13-18. Like Mr. Moul, he used a proxy group of publicly traded water companies. *Id.* Other than the exclusion of Artesian Water Resources Corp., Mr. Rothschild's proxy group was identical to Mr. Moul's group. *Id.*

As noted, Mr. Rothschild used a Constant Growth DCF. He stated the Constant Growth

DCF is used to determine the ROE¹² when investors can reasonably expect the growth of retained earnings and dividends to be constant. Tr. p. 194.42, ll. 8-18. The result of his DCF analysis using the Constant Growth form of the DCF indicated an ROE range between 8.05% and 8.15% for his proxy group. Tr. 194.8, ll. 16-19. Mr. Rothschild's Non-Constant Growth DCF is meant to determine the return on investment expected by investors based on the estimated annual cash flows an investor expects to receive over a fixed period. Tr. p. 194.49, ll. 13-15, The cash flow at the end of the ten-year forecast period consists of both the last year's dividend forecast by Value Line, and the estimated proceeds from the sale of the stock. Exhibit ALR-3, p. 4. Mr. Rothschild's Non-Constant Growth DCF resulted in a cost of equity between 5.80% and 6.03%. Tr. p. 194.54, ll. 5-8.

Mr. Rothschild testified that the biggest difference between his DCF calculations and those of Mr. Moul is growth formula. Mr. Rothschild uses a mathematical formula ("b x r") to forecast the growth rates of the proxy group, while Mr. Moul relies on analysts' forecasts. Tr. pp. 194.87-194.91.

Mr. Rothschild's CAPM analysis was varied. He reported a Weighted Average CAPM using hybrid betas and forward-looking betas with a three-month treasury bill risk free rate, yielding a range of 6.04% to 6.76%, and 6.68% to 7.25% using a thirty-year treasury bond as the risk-free rate. Tr. p. 194.84. His Spot CAPM yielded 6.22 % for with three-month treasury bill and 6.81 with a thirty-year treasury bill risk free rate. *Id.*

¹² Mr. Rothschild uses the term "cost of equity" ("COE") as opposed to "return on equity" ("ROE"). The two terms mean the same thing for purposes of this discussion, and the Commission will use ROE throughout this order for consistency.

The ORS expert witness, David J. Garrett, recommended an ROE of 8.9%. Mr. Garrett testified that his objective cost of equity analysis reflected a cost of equity of about 7.1% within a range of 6.3% to 8.0% (Garrett prefiled direct, Tr. p. 7, ll 4-16). Mr. Garrett explained that the legal standards governing a determination of ROE do not mandate that the ROE equate to the result of a particular financial model but that it be reasonable under the circumstances. Mr. Garrett testified that the circumstances surrounding Palmetto's rate application were "unique" and adopting an 8.9% ROE would permit the Commission to gradually but meaningfully lower Palmetto's ROE to cost. *Id.* Mr. Garrett performed a DCF and CAPM analysis. By modeling the DCF formula using the known inputs of stock price and dividends and his subjective growth rate input, Mr. Garrett's DCF Model cost of equity estimate was 8.0% (Garrett prefiled direct, Tr. p. 268.46, l. 1). Mr. Garrett also modeled the CAPM analysis, which assesses risk-based return. (Garrett prefiled direct, at p. 48, ll. 6-8). Mr. Garrett testified that he estimated Palmetto's CAPM cost of equity to be 6.3% (Garrett prefiled direct, Tr. p. 268.58, ll. 5-7). Averaging the results of his two models, Mr. Garrett arrived at a cost of equity for PWR of 7.1%. (Exhibit DJG-12).

However, Mr. Garrett advocated against setting Palmetto's ROE at 7.1%. He explained that awarding a return of 7.1% in the current rate proceeding would represent a substantial decrease from ROEs historically awarded to South Carolina public utilities. For this Commission to make a significant, sudden change in the ROE anticipated by stockholders would have the unanticipated and undesirable effect of notably increasing [Palmetto's] risk profile in contravention of the *Hope* Court's end result doctrine. Mr. Garrett opined that an ROE of 8.9% represented a good balance between the Supreme Courts' holdings that awarded ROEs should be based on cost, while requiring the resulting ROE to be just and reasonable under the circumstances. Mr. Garrett testified that an ROE of 8.9% represents a gradual, yet decisive move toward PWR's market-based

cost of equity, while still providing PWR's shareholders with the opportunity to earn a return in excess of his market-based cost of equity. (Garrett prefled direct, Tr. at p. 268. 12, l. 3 – p. 13, l.3).,

The Commission has wide latitude in selecting a rate-setting methodology. *Heater of Seabrook, Inc. v. Public Service Comm'n*, 324 S.C. 56, 64, 478 S.E. 2d 826,830 (1996). The Commission was presented with a wide range of ROE recommendations. Unsurprisingly, the Company's expert witness recommended the highest ROE (10.95%) while the DCA and ORS experts recommended much lower ROEs (7.31% and 8.9% respectively). The record supports an ROE somewhere between these extremes.

There is no dispute that Palmetto is a well-run company. Only one of the Company's customers appeared at the public hearing in this case, and she had no service-related complaints. Tr. pp. 71, l. 19 – 72, l. 25. Palmetto has had no serious environmental issues, and it has contributed to the betterment of the community. The Company's high quality of service should not be taken for granted. The Commission's determination of the appropriate ROE is not only a reflection of market conditions, but also a signal to the regulated utility community and the public at large. With only a single exception, the Commission has not awarded an ROE lower than 9.0% in the past ten years.¹³ Mr. Moul testified that an ROE of 9.5% was in the range or return expected by investors in this jurisdiction and that a departure from an ROE range in the mid-nines would be concerning to investors. (Tr. P. 160, L. 16 - P. 162, L. 23) Mr. Garrett testified to as much when he opined that a reduction in Palmetto's ROE must be gradual. Mr. Sorensen testified that from a practical standpoint, he would have to compete for capital with other utilities with authorized ROEs in

¹³ See Water and Wastewater Rates, <https://psc.sc.gov/consumer-info/water-and-wastewater-rates>

excess of 9%. Tr. pp. 69, l. 2-70, l.3; 75.4, l. 3-7. Under the circumstances an ROE of 9.5% for Palmetto would be just and reasonable and would equitably balance the interests of ratepayers and investors. (Tr. P. 160, l. 16 – p. 162. L. 23).

Commission Finding

Based on the totality of the evidence, the Commission finds an ROE of 9.5% is appropriate for Palmetto. With the above approved ROE of 9.5% the Commission finds and adopts the resulting total Revenue Requirement for Palmetto of \$3,958,911 which is an increase of \$265,236 in revenues. This represents an approximate 53% reduction from the Company's requested increase of \$499,003 made in its Application. Additionally, the resulting Operating Margin of 15.19% is found to be just and reasonable and is adopted by the Commission for Palmetto in accordance with S.C. Code Ann. §58-5-240(H).

IV. FINDINGS OF FACT AND CONCLUSIONS OF LAW

Based upon the discussion as set forth herein, and the record of the instant proceeding, the Commission makes the following Findings of Fact and Conclusions of Law:

1. PWR is a wastewater utility providing sewer service in its assigned service area located in Richland and Lexington Counties. The Commission is vested with authority to regulate rates of every public utility in this state and to ascertain and fix just and reasonable rates for service. S. C. Code Ann. § 58-5-210 *et. seq.* PWR's operations in South Carolina are subject to the jurisdiction of the Commission.
2. PWR is a wholly owned subsidiary of Ni South Carolina, Inc., which is a subsidiary of South Carolina Utility Systems, Inc, which is a subsidiary of Southeast Utility Systems, Inc., which is a subsidiary of SouthWest Water Company.

3. The appropriate Test Year period for this proceeding, selected by PWR, is January 1, 2020, to December 31, 2020. PWR submitted evidence in this case with respect to its revenues and expenses using a Test Year consisting of 12 months ending December 31, 2020.
4. The Commissions finds, for the reasons discussed above, that the Stipulation entered into by the Parties and attached to this Order as Exhibit 1 is fair, just, and reasonable for PWR and its customers. Therefore, this Commission adopts the Stipulation in its entirety.
5. The Commission finds that the adjustments and customer protections as discussed in the Stipulation and previously in this Order are just and reasonable and the Commission hereby adopts and approves the same.
6. [Sentences regarding ROE]. The Commission also finds that the cost of debt of 3.79% and a capital structure consisting of 45% debt and 55% equity to which the Parties agreed in the Stipulation is just and reasonable. All of these figures are supported by the reliable, probative, and substantial evidence on the whole record and are in the public interest.

IT IS THEREFORE ORDERED THAT:

1. PWR is authorized the opportunity to earn an ROE of 9.5%.
2. PWR's capital structure is 45% debt and 55% equity.
3. PWR's cost of debt is 3.79%.
4. The Stipulation executed by the Parties is accepted and adopted in its entirety, including the adjustments and rate schedule language changes described therein.
5. As set forth in the Stipulation, the customer protections Witness Garrett proposed are approved. It is, therefore, ordered:
 - PWR will not seek recovery of any goodwill associated with the Acquisition in any future rate proceedings;

- PWR will not seek to recover any acquisition or transaction costs associated with the Acquisition in any future rate proceedings;
- PWR will not in any way be the guarantor of any debt for SWWC or any SWWC affiliate or subsidiary entities unless the debt is incurred for purposes specific to the PWR system and operations;
- Any debt incurred by PWR is and will only be used for purposes specific to the PWR system; and
- PWR will not lend cash or any other capital directly to SWWC or any SWWC affiliate or subsidiary entities except for routine and prudent cash management practices.

6. PWR's rates shall be set using the rate base methodology; with a return on rate base of 6.93% based upon a return on equity of 9.5% and a capital structure of 45% debt and 55%.

7. Pursuant to S.C. Code Ann. § 58-5-240(H), PWR's operating margin is 14.42% as reflected in Order Exhibit 2.

8. PWR shall file a schedule showing the revenue produced by each and every tariffed rated approved by the Commission and reconcile the revenue produced, by tariffed rate, to the revenue requirement approved in this Order. This schedule must detail the revenues, expenses, and rate base components used to calculate the Commission approved revenue requirement.

9. The revenues resulting from this Order are fair and reasonable and will allow PWR to continue to provide its customers with safe and reliable wastewater service.

10. PWR shall charge the rates approved herein for service rendered after the date of this order. The schedules will be deemed filed with the Commission under S.C. Code Ann. § 58-5-240.

11. Revised tariffs shall be filed within ten (10) days of receipt of this Order, consistent with the Commission's Rules and Regulations. The tariffs should be electronically filed in a text searchable PDF format using the Commission's DMS System (<https://dms.psc.sc.gov>). An

additional copy should be sent via email to etariffpsc.sc.gov to be included in the Commission's ETariff System (<http://etariff.psc.sc.gov>). Future revisions should be made using the ETariff System. The tariffs shall be consistent with the findings of this Order and agreements with the other parties to this case. The Company shall provide a reconciliation of each tariff rate change approved as a result of this order to each tariff rate revision filed in the ETariff System. Such reconciliation shall include an explanation of any differences and be submitted separately from the Company's ETariff System filing. The rates, fees, and charges in the revised tariffs shall be consistent with the adjustments as stipulated between the Parties and the 8.9% ROE authorized in this Order.

12. The Company's books and records shall continue to be maintained according to the NARUC Uniform System of Accounts.

13. PWR shall maintain a performance bond for sewer operations in the amount of \$350,000 in compliance with S.C. Code Ann. § 58-5-720.

14. This Order shall remain in full force and effect until further Order of this Commission.

BY ORDER OF THE COMMISSION:

Justin Williams, Chairman

ATTEST:

Florence P. Belser, Vice-Chairman